



# FDI and Economic Growth in Developing African economy: A study of FDI inflows to different Sectors of Nigeria

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## General Note



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## ABSTRACT

This study evaluates the influence of Foreign Direct Investment on Economic growth of different sectors developing African economy. FDI is an important factor that channel funds to key sectors developing economy like Nigeria. The main objective of the study is to evaluate the influence of FDI to different sectors on economic growth of Nigeria. The specific objectives of this study is to examine the relationship between FDI to agriculture, banking and manufacturing sectors and economic growth of developing

African economy (Nigeria). The study used secondary data obtained from Central Bank of Nigeria Statistical Bulletin of various years and subjected them to ADF stationarity test, co-integration and multiple linear regression study to analyse the study over the period of 1986 to 2018. The findings of the study showed that FDI to agriculture, banking and manufacturing sector improve economic growth position both in the short run and long run significantly. The study therefore concludes that FDI to the different sectors of the economy significantly influence economic growth of developing African economy in Nigeria. Hence, the study recommends reduction of bottlenecks that frustrate foreign investment to the agricultural sector, manufacturing sector and the banking sector of Nigeria to foster enhanced investment frontiers in the key sectors of the economy and economic growth at large.

**Keywords:** FDI, Economic growth, GDP, Agriculture, Manufacturing, Banking

## 1. INTRODUCTION

Foreign Direct Investment is in the center of developing nations economic growth objectives. The ever-increasing demands and sourcing of foreign investment has caused many nations to continuously demand partnership in the form of bilateral relations to foster improved economic growth and enshrine improved sectoral development of nations. Developing economies in Africa are basically providing more policy friendly environment to attract further investment in key sectors like the capital market, agricultural sector, manufacturing, textiles industry, oil sector, gold mining, banking sector, communication, education and so on. However, the level of economic growth compared to the evolving foreign investment expansion has raised serious questions as to the possible impact of foreign direct investment on the economic growth of developing economies like Nigeria. For instance, foreign direct investment in Nigeria showed an average of \$1279.72 US million Dollars between 2007 to 2018, reaching an all-time high of \$3084.49 US million Dollars in the fourth quarter of 2012 and a record low of \$435.64 US million Dollars in the second quarter of 2018 (CBN, 2018). However, despite the increased flow of foreign direct investment into Nigeria, there is still low growth rate of GDP, increase in unemployment rate and depleted per capita income; thus, questioning the theoretical role of foreign direct investment increase in the Nigerian economy. This inconsistency in the theoretical disposition of foreign direct investment on the economic growth of Nigeria has previously been examined at a larger scale in a multiple countries study (Hanson, 2001; Lumbila, 2005, Jenkins & Thomas, 2002; Uwubanmwen & Ogiemudia, 2016). Majid and Elehe (2016) believed that the relationship between foreign direct investment and economic growth is definitely country and period specific. Hence, this study seeks to identify the relationship between foreign direct investment to key sectors of the economy and the economic growth of Nigeria.

### Review of Related Literature

Different theories discuss the components of foreign direct investment in an economy. For instance, the endogenous growth theory holds that economic growth is primed on investment in human capital, innovation and knowledge diffusion (Paul Romer, 1986; Robert Lucas, 1988; Sergio Rebelo, 1991; Romer, 2008; Lucas, 2004, Barro & Sala-i-Martin, 2007). The neoclassical theory also holds that FDI via technological transfers and spillovers, research and development (R&D) and human capital influences income growth by increasing the amount of capital per person (Adam Smith (1723-1790) and David Ricardo (1772-1823), Mundell (1957) further highlight the neoclassical trade theories, Kindleberger, 1969; Hymer, 1960). These theories however discuss the components of foreign direct investment as it improves economic growth which were reflected in previous studies like Adigwe, Ezeagba and Udeh (2015), Mori, Jaratin, Rozilee, Dullah and Nanthakumar (2012), Heang and Moolio (2013), Kogid, Mulok, Beatrice and Mansur (2010), Karimi and Yusop (2009), Roy and Berg (2006) and Duasa (2007) discovered mixed effect of foreign direct investment on economic growth. For instance, Mori, Jaratin, Rozilee, Dullah and Nanthakumar (2012) in Malaysia, Adigwe, Ezeagba and Udeh (2015) in Nigeria, Muntah, Khah, Halder and Ahmad (2015) in Pakistan, Roy and Berg (2006) in US economy having significant effect while Kogid, Mulok, Beatrice and Mansur (2010), Karimi and Yusop (2009) and Duasa (2007) showed insignificant effect. This insignificant position is corroborated in the study of Thailand by Ang (2008). Nigerian study in Onu (2012) showed that FDI does not affect economic growth between 196 to 2007 while Omankhanlen (2011) and Onakoya (2012) showed significant effect of FDI to different sector on economic growth. However, OLS study in Nigeria also revealed mixed results as Olokoyo (2012), showed insignificant relationship while Adeleke, Olowe and Fasesin (2014), Shaibu, Osemwengie and Oseme (2014) revealed significant relationship in the face of unfavourable economic situations.

However, a multiple country study in Caudros, Orts and Alguancil (2004), Makki and Somwaru (2004), Herzer, Klasen and Nowak-Lehmann (2008), Lumbila (2005) and Adewunmi (2006) in Africa, Eryigit (2012), Sridharan, Vijayakumar and Chandra (2009) and Sandalcilar and Altiner (2012) showed significant effect of foreign direct investment on economic growth. Anowar and Mohammad

(2012), Chowdhury and Mavrotas (2006), Nishiyama and Yamaguchi (2010), Hameed and Bashir (2012), Agrawal(2015) and Qiaser, Salman, Ali, Hafiz and Mohammad (2011) also discovered significant effect of FDI on economic growth.

The real GDP is found to be a major instigator of FDI inflows (Mori, Jaratin, Rozilee, Dullah & Nanthakumar, 2012; Nosheen, 2013) in Pakistan. Earlier study in Nuzhat (2009) held that FDI was no instigator of economic growth in Pakistan.

Mori, Jaratin, Rozilee, Dullah and Nanthakumar (2012) study of FDI and economic growth in Malaysia between 1971 to 2009 discovered the existence of a long-run co-integration relationship between FDI and RGDP. FDI also granger cause changes in RGDP implying that FDI influence economic growth. Another Malaysia study in Duasa (2007) study of Foreign Direct Investment and Growth discovered no causal relationship between FDI and economic growth (GDP). Studies like Herzer, Klasen and Nowak-Lehmann (2008), Kogid, Mulok, Beatrice and Mansur (2010) and Karimi and Yusop (2009) support these findings with no causal effect of FDI on GDP at different studies. Ang (2009) studied Foreign Direct Investment and Its Impact on the economic growth of Thai economy and revealed that FDI negatively affected economic growth.

Sridharan, Vijayakumar and Chandra (2009) examined the causal relationship between FDI and economic growth of the BRICS countries from 1992 to 2007. Their study discovered that BRICS countries have co-integration relationship. They also discovered that Brazil, Russia and South Africa had bidirectional causal effect between FDI and GDP while India and China showed a one-way causal effect from FDI to GDP in the two countries. The study of the impact of FDI inflows on United States economy between 1970 to 2001 by Roy and Berg (2006) found that FDI have a significant, positive, and economically important impact on U.S. economic growth.

Sandalcilar and Altiner (2012) investigate the Foreign Direct Investment and Gross Domestic Product in ten Economic Cooperation Organization (ECO) member countries from 1995 to 2011. Their study discovered a strong positive causality from FDI to GDP and a slightly less positive causality from GDP to FDI in ECO region. Heang and Moolio (2013) examined foreign direct investment and gross domestic product of Cambodia in long run over the period of 1993-2011, and discovered a long run positive relationship between FDI and GDP in Cambodia. Qaiser, Salman, Ali, Hafiz and Muhammad (2011) investigate the impact of foreign direct investment on Growth (GDP) from year 2001 to 2010 of SAARC Countries and discovered that there is a positive and significant relationship between FDI and GDP.

The study of the impact of FDI on GDP in MENA countries by Hameed and Bashir (2012) revealed that FDI leads to Economic Growth and this impact varies by region. Yamaguchi (2010) also investigated FDI inflows from developed countries to developing countries and their result indicated that FDI leads to an increase in GDP of developing countries. The result is supported by findings of Eryigit (2012).

Thus, looking at the mixed position in the empirical review and limited position of study on FDI to different sectors of the economy and economy growth. This study examines the relationship between FDI to agriculture, banking and manufacturing sectors of Nigeria and economic growth.

## 2. METHODOLOGY

The research question and objectives of the study is model to identify the relationship between the dependent variable (RGDP) and independent variables (FDI to AGRIC, BANKING and MANUFACTURING) and the research design used is *ex post facto* research design and collected data from CBN statistical bulletin of various years. This study is modeled after the impact of FDI on GDP in different sectors of Nigeria by Onakoya (2012).

Our study is modeled thus;

$$Y = F(X_1, X_{2t-1})\mu \text{-----equation (1)}$$

Where;

$X$  = Inflow of FDI (FDIA, FDIB, FDIM);

$Y_1$  = Real GDP;

$\mu$  = error term.

$$RGDP = \beta_0 + FDIA \beta_1 + FDIB \beta_1 + FDIM \beta_1 + e_t \text{..... (2)}$$

Where;

RGDP= Real Gross Domestic Product, FDIA= Foreign Direct Investment inflow in Agriculture, FDIB= Foreign Direct Investment inflow in Banking sector, FDIM= Foreign Direct Investment inflow in Manufacturing,  $\beta_0$ = Constant,  $\beta_1$  = Intercept and  $e_t$  = Error Term

The study is however subjected to stationary test, Co-integration test and Multiple regression.

### 3. RESULT AND DISCUSSION OF FINDINGS

**Table 1: Unit Root Tests using Augmented Dickey Fuller**

Variable	ADF Test	C. Values @5%	P-value	Order of Integration	Decision
FDIA	-7.619133	-2.948404	0.0000	1(2)	Stationary
FDIB	-4.895249	-2.945842	0.0003	1(1)	Stationary
FDIM	-2.753611	-1.950687	0.0073	1(2)	Stationary
RGDP	-6.461532	-2.948404	0.0000	1(2)	Stationary

Source: Summary of E-view 10.0 Output

The stationarity outcome in table 1 showed that the tests for stationarity properties of the series (all the variables) following the Augmented Dickey Fuller (ADF) statistics were found to be stationary at, order one (1) and (2). At the First and Second difference as reported, the ADF statistics for the respective variables were all negative and significant at the critical values of 5% significance level and the Null Hypothesis of the presence of unit root in all the variables is convincingly rejected for variable FDIA, FDIB, FDIM and RGDP. Hence, the variables are stationary and good for analytical purposes.

**Table 2: Cointegration Test Result @ 5% level**

Date: 12/24/19 Time: 14:09				
Sample (adjusted): 1983 2018				
Included observations: 36 after adjustments				
Trend assumption: No deterministic trend (restricted constant)				
Series: RGDP FDIA FDIB FDIM				
Lags interval (in first differences): 1 to 1				
Unrestricted Cointegration Rank Test (Trace)				
Hypothesized	Trace		0.05	
No. of CE(s)	Eigenvalue	Statistic	Critical Value	Prob.**
None *	0.678367	85.68334	54.07904	0.0000
At most 1 *	0.487184	44.84700	35.19275	0.0034
At most 2 *	0.356655	20.80485	20.26184	0.0421
At most 3	0.127888	4.926164	9.164546	0.2916
Trace test indicates 3 cointegrating eqn(s) at the 0.05 level				
* denotes rejection of the hypothesis at the 0.05 level				
**MacKinnon-Haug-Michelis (1999) p-values				
Unrestricted Cointegration Rank Test (Maximum Eigenvalue)				
Hypothesized	Max-Eigen		0.05	
No. of CE(s)	Eigenvalue	Statistic	Critical Value	Prob.**
None *	0.678367	40.83634	28.58808	0.0009
At most 1 *	0.487184	24.04215	22.29962	0.0283
At most 2	0.356655	15.87869	15.89210	0.0502
At most 3	0.127888	4.926164	9.164546	0.2916
Max-eigenvalue test indicates 2 cointegrating eqn(s) at the 0.05 level				
* denotes rejection of the hypothesis at the 0.05 level				
**MacKinnon-Haug-Michelis (1999) p-values				

Source: E-view 10.0 Output

The cointegration result for the study in table 3 of the trace and maximum Eigen-value tests shows the existence of three (3) co-integrating vectors (p-value of 0.0000, 0.0034, 0.0421 for trace test and 0.0009, 0.0283 and 0.0502 for maximum eigenvalue) between FDIA, FDIB, FDIM and RGDP at the 5% level of significance. This thus confirms the existence of long-run equilibrium (co-integration) effect of FDIA, FDIB and FDIM on RGDP.

**Decision rule:** We reject null hypothesis of the co-integration relationship to accept the alternative that there is Co-integration. We thus, conclude that FDI investment to the economic segment of FDIA, FDIB and FDIM have long-run equilibrium effect on economic growth in RGDP.

**Table 3: Multiple Regression Result**

Dependent Variable: RGDP Method: Least Squares Date: 12/24/19 Time: 14:27 Sample (adjusted): 1982 2018 Included observations: 37 after adjustments				
Variable	Coefficient	Std. Error	t-Statistic	Prob.
FDIA	4.122723	0.306747	13.44016	0.0000
FDIB	-7.481461	2.479094	-3.017821	0.0050
FDIM	-2.106971	0.607566	-3.467888	0.0015
ECM2(-1)	1.024705	0.133209	7.692457	0.0000
C	18421.90	491.9447	37.44709	0.0000
R-squared	0.988698	Mean dependent var		34224.35
Adjusted R-squared	0.987285	S.D. dependent var		19601.52
S.E. of regression	2210.287	Akaike info criterion		18.36472
Sum squared resid	1.56E+08	Schwarz criterion		18.58241
Log likelihood	-334.7473	Hannan-Quinn criter.		18.44147
F-statistic	699.8230	Durbin-Watson stat		1.287468
Prob(F-statistic)	0.000000			

Source: E-view 10.0 Output

In table 3, the  $R^2$  and Adjusted  $R^2$  both showed 98.87% and 98.73% respectively. This shows that the chosen regression model best fits the data. Hence, the goodness of fit regression model is 98.87% and implies that chosen explanatory variables explain variations in the dependent variables to the tune of 98.87%. Also, with a high Adjusted  $R^2$  (98.73%) implies that the model can take on more variables conveniently without the  $R^2$  falling beyond 98.87%, which is very high. F-statistics of 699.8230 is considered very good being positive and significantly large enough and it shows that there is significant positive relationship between the dependent and explanatory variables. The P-value of (F-statistics) 0.00000 is rightly signed and very significant and displays a Durbin-Watson of 1.287468 is considered good but show the presence of autocorrelation on the chosen data. Hence, the presence of autocorrelation necessitated the need for confirmatory test as shown in table 4.

However, the components of FDIs to the agriculture sector, banking sector and manufacturing sector have t-statistic value of 13.44016, -3.017821 and -3.467888 with p-values of 0.0000, 0.0050 and 0.0015 respectively was found to have a significant relationship economic growth and this impact is both positive and negative for Agriculture and banking and manufacturing respectively at 5% significance level since its p-value is well below 0.05.

The findings showed that foreign direct investment to the different sectors of the Nigerian economy in FDIA, FDIB and FDIM were able to significantly improved economic growth in Nigeria within the period under review. The outcome registered that foreign direct investment is a stimulator of key economic activities in Nigeria as shown in the roles of the investment in the different segment of the economy in agriculture, banking and manufacturing. Regardless of the presence of autocorrelation, the confirmatory tests affirm to the reliability of the findings of the study. Thereby, stating that FDI to these sectors of the economy boosted economic activities both positively and negatively and the economic growth at large.

## Serial Autocorrelation

**Table 4: Result of the test for BG Serial Correlation**

Breusch-Godfrey Serial Correlation LM Test:			
F-statistic	4.083732	Prob. F(2,30)	0.0270
Obs*R-squared	7.917639	Prob. Chi-Square(2)	0.0191

Source: E-view 10.0 Output

The result of the BG serial correlation shows that the probability value is 0.0270, which is less than 0.05 implying that we reject  $H_0$  and accept  $H_1$ . Thus, confirming the absence of autocorrelation. However, further test is conducted in Heteroskedasticity test for affirmation of autocorrelation or its non-existence and reliability of findings for decision.

**Table 5: Result of the test for Heteroskedasticity Serial Correlation**

Heteroskedasticity Test: ARCH			
F-statistic	1.672414	Prob. F(1,34)	0.2047
Obs*R-squared	1.687772	Prob. Chi-Square(1)	0.1939

Source: E-view 10.0 Output

The result of the Heteroskedasticity serial correlation shows that the probability value is 0.2047, which is greater than 0.05 implying that we reject  $H_0$  and accept  $H_1$ . We therefore conclude that there is no serial autocorrelation in the model and that the model is appropriate.

**Decision:** The study therefore reject the null hypothesis of no significant relationship between FDIA, FDIB and FDIM and RGDP therefore accepting the alternative of a significant relationship between FDIA, FDIB and FDIM and the RGDP in Nigerian within the period under review.

## 4. CONCLUSION AND RECOMMENDATION

The results emanating from our study proved that FDI to the different sector of the economy in agriculture, banking and manufacturing grossly impacted economic growth of Nigeria significantly within the period under review in line with the findings of previous single country studies in Adeleke, Olowe and Fasesin (2014), Saibu and Keke (2014) significant relationship in the face of unfavourable economic situations and multiple countries study in Anowar and Mohammad (2012), Chowdhury and Mavrotas (2006), Nishiyama and Yamaguchi (2010), Hameed and Bashir (2012), Agrawal (2015) and Qiaser, Salman, Ali, Hafiz and Mohammad (2011). A long-run relationship was also established and documented appropriately for FDI in Nigeria. Conclusively, in line with the outcome of the study, FDI to the different sectors of the economy significantly influence economic growth of developing African economy in Nigeria.

The study recommends among others that government should reduce bottlenecks that frustrate foreign investment to the agricultural sector, manufacturing sector and the banking sector of Nigeria to foster enhanced investment frontiers in the key sectors of the economy and economic growth at large. Above all, considerate efforts of FDI should be channeled towards the banking sector as to facilitate the chances of banks to extend more credit facilities into the economy and boosting the economic activities and growth.

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## Conflicts of Interest

None



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